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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1940.

No. 8.

CRANE-JOHNSON COMPANY, a Corporation of North Dakota,
*Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

## MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF AMICUS CURIAE.

THOMAS H. REMINGTON,
Rochester, N. Y.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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## MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE.

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Comes now the undersigned and moves for leave to file a brief amicus curiae in the above-entitled case on behalf of Bastian Brothers Company. This brief is submitted herewith. The requisite consents having been filed with the Clerk.

THOMAS H. REMINGTON,
Rochester, N. Y.

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## BRIEF AMICUS CURIAE.

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*May It Please The Court:*

If the word "contract" in Section 10 of Article 1 of the Constitution embraces a corporate charter then the unqualified word "contract" also embraces a corporate charter when used in an ordinary statute—no contrary intention appearing.

At the bottom of page 17 and the top of page 18 of the Government's brief we understand this to be conceded. At page 18 of the Government's brief it is also conceded "that laws which exist at the time of the making of a contract and which affect its validity, construction, discharge, or enforcement enter into and form a part of the contract as though they were incorporated in its terms."

From this concession it follows that the provision of the statute of North Dakota which expressly deals with the pay-

ment of dividends and expressly prohibits them is as much a provision of the charter contract as though it were "incorporated in its terms."

## Point I.

In the second paragraph on page 18 of its brief the Government makes for its first point that the charter contract was not "executed" by the corporation because "executed" means signed. Obviously this argument cannot be used against a stock certificate. Hence it is out of the *Northwest Steel Rolling Mills* case.

It is stated in Contracts, 17 C. J. Secundum, Sec. 7, p. 326 that the word "executed" often means "made." We submit it means "made" in this statute. Necessarily there are at least two parties to every contract and necessarily both of them make it. Moreover Congress in using this phrase of the law had only in mind the time within which a contract must be made, and that it be in writing. This is obvious from statements in Committee reports quoted on page 23 of Crane-Johnson brief. *There was no reason for attaching any significance to the word "executed."* On the other hand there was every reason for requiring the contract prohibition to antedate May 1, 1936. Otherwise few corporations would have paid any tax. As stated in the Government's brief in the *Northwest Rolling Mills* case the requirement of a written contract was to guard against unscrupulous taxpayers.

## Point II.

The second argument of the Government is stated as follows:

> "The most obvious and rational meaning of the words 'a provision of a written contract is a provision expressly written into the contract and not one that is implied.'"

Of course the use of the bald phrase "the most obvious and rational meaning of the words" adds nothing to the

reason of the Government's argument. We deny that this is their obvious and rational meaning. *The statute does not say what the Government asks the court to read it to say.* If Congress had intended to say that, it had facility of expression enough to say it. The lawyers in Congress knew that the State law was a part of the corporate charter and also a part of the stock certificate contract. If they had not desired this principle of law to have full effect they would have phrased the statute differently.

Four rules of construction support the point that the statute should not be construed to require the conceded provision of the contract (Government's brief, page 18) which expressly deals with the payment of dividends to be expressly recopied into the contract. These rules are:

(1) The rule that regards the spirit and purpose of a statute in determining its meaning.

(2) The rule that substance and realities control over form in tax cases.

(3) The rule that doubts in the construction of tax laws must be resolved in favor of taxpayers.

(4) The rule requiring a liberal construction of a relief provision of a tax statute.

**Point III.**

The third argument of the Government on page 20 is that the prohibition is only on the directors and not on the corporation. A corporation cannot act except through human beings and a prohibition on the only human beings who can do the act for the corporation is necessarily a prohibition on the corporation itself. The Supreme Court of North Dakota has so construed this statute. See page 15, Crane-Johnson Company brief.

**The Board of Tax Appeals Misapprehended the Legislative History.**

In addition to reasons set forth in the brief for petitioner why the Board of Tax Appeals misapprehended the legislative history, the following is submitted:

The United States Board of Tax Appeals reaches the conclusion that the failure to include a provision in the Revenue Act of 1936 similar to Section 14 of the original house bill was an expression of deliberate intent by Congress not to give relief to deficit corporations. Exception is taken to this conclusion in that it appears from the legislative history that such a conclusion cannot be reached. The intent of Section 14 of the original house bill is best expressed by the following quoted language from Par. XIX in the Report of the Subcommittee of Ways and Means issued under date of March 26, 1936:

> "It is recommended that relief be provided for the corporation which, while having an adjusted net income for the taxable year, lacks sufficient accumulated earnings and profits as of the close of the taxable year from which to distribute *taxable* dividends equal to the adjusted net income." (Italics ours)

The use of the word "taxable" shows this related only to deficit corporations legally able to pay dividends. No others would distribute.

Thereafter in this report examples are quoted, all of which express the hardship which would be suffered by those corporations having accumulated earnings of an amount less than the adjusted net income for one reason or another. Under the existing definition of a dividend as contained in Section 115(a) of the house bill and prior revenue acts, dividends were taxable to shareholders only to the extent that they were paid out of accumulated earnings or profits, so that any corporation actually paying dividends in excess of such earnings and profits would not

receive the dividend paid credit, because the credit provision required a taxable dividend. The recommendation of the Subcommittee on Ways and Means in order to remedy this situation was practically identical with the wording used in Section 14 of the house bill, but the expressed intent of this section was to relieve those corporations which though legally permitted to pay dividends, would not receive the dividend paid credit.

This situation was entirely remedied in the Senate by Section 115(a) of the revenue act of 1936 wherein the definition of a dividend was so changed as to permit a dividend credit for those corporations actually paying dividends if the year's earnings and profits were in excess of such dividends, without regard to the accumulated earnings and profits. Of course this related only to deficit corporations who could legally pay dividends. It was assumed the others would observe the law, and not pay any.

Thus the purpose and intent of Section 14 of the house bill was entirely accomplished in the Senate by the change of the definition of a dividend and it was for this reason that Section 14 of the house bill was not included in the revenue act of 1936.

It is therefore our position that the United States Board of Tax Appeals erred in the case at bar in reaching the conclusion that the failure to include Section 14 of the house bill in the revenue act of 1936, was an expression of deliberate intent not to give relief to any deficit corporations. The only intended relief of Section 14 was that expressed by the Subcommittee of Ways and Means, and this relief was granted by the revenue act of 1936 through the changed definition of a dividend. Section 15 took care of deficit corporations prohibited by charter contract from declaring dividends and it was retained and liberalized.

When the Senate determined to reduce the tax on them to 7 per cent and make relief from it for these corporations conditional upon the distribution of dividends by them it

was necessary to change the definition of a dividend, or such corporations would have had no relief even if they did distribute dividends. This change in the definition of a dividend had nothing to do and did not relate to corporations forbidden by law to distribute dividends. They were taken care of by the contract clause of the statute.

To say that the Senate struck out section 14 to deliberately deny relief to deficit corporations is a speculation which will not square with these facts. The House bill imposed exactly the same flat tax (15 per cent) on undistributed income of deficit corporations which could pay dividends and on undistributed income of corporations forbidden by contract to pay dividends. The Senate bill cut the tax on deficit corporations legally able to pay dividends to 7 per cent and entirely relieved corporations under contract not to pay dividends from the tax. Even deficit corporations legally able to pay dividends were better off under the Senate bill than under the House bill. The Senate bill taxed undistributed income 7 per cent and gave an election to avoid that by distributing income.

**Reply to the Reasoning of the Decisions Below.**

The proposition for consideration then is: Does the contract involved in this case conform to and comply with the provisions of Section 26 of the Revenue Act of 1936 and so afford appellant the relief it sought in this action? It is our position that it does.

Certainly the title of 26(c)(1) "PROHIBITION ON PAYMENT OF DIVIDENDS" is broad and direct enough to include the credit appellant contends for here. If that be true why should the text of the subsection, having to do with a single provision of a contract, be limited to a point where it works a hardship upon a corporation at a time when it is in no financial condition to be dealt a blow.

The all important "provision" of the contract described in the subsection in question is a provision of a written contract executed by the corporation prior to May 1, 1936,

which provision expressly deals with the payment of dividends.

Now the first point we affirm is, by way of summary for the argument heretofore submitted, that the charter of this taxpayer and the applicable statutes of the State of North Dakota taken together constitute a written contract. The charter is in writing—the statutes are in writing. The entire contract is in writing and complete just as much as if in the drawing of a written contract the draftsman were to provide that certain facts of a certain paragraph "were further exemplified as set out in Exhibit A (a set of specifications) attached hereto and made a part of this contract." The only thing possible of implication is something not expressly set out in the charter or the statutes which is reasonably necessary to the carrying out of the purposes and objectives of the corporation.

Our reason for making the point of what may be implied is because in *Crane-Johnson Co.* v. *Commr. Inter. Rev.*, 105 F. (2d) 740, the court in considering this point said:

> "These statutes, we think, do not establish a contract executed by the corporation expressly dealing with the payment of dividends. *If there is such a contract, it is not an express one, but is implied.*"
>
> "Such contract as arises from the organization of a corporation under state laws is an implied rather than a voluntary written agreement entered into by the corporation."

The mere statement of what the court said against what Section 26 (c)(1) states shows where the court missed the scent of its quarry.

We do not say that "These statutes" establish a contract executed by the corporation expressly dealing with the payment of dividends. What we say is, that the statutes in question constitute "a provision of a written contract * * * which provision expressly deals with the payment of dividends."

It is our further contention that the expression of the court "If there is such a contract it is implied" decides

nothing. Interpreted strictly it says, that if one were to say that "these statutes" were "such a contract" it, the contract, is implied. The statutes are not implied nor can be. They are written and of record. But granted that what the court meant to say was that to make a contract out of the charter and the statutes one had to imply that they were to be taken together, still the court will have said nothing relevant to the point involved in this case because:

The clauses of the section involved here do not provide against the contract in question gaining force by implication. What it does say is that the contract relied upon by the taxpayer shall be a written contract, as this one is, even though it might be said that the two parts are brought together by implication. And then it goes on to say that the "provision" of that written contract shall be one that "expressly deals with the payment of dividends." We submit that the statutes are in writing; that they are one of the provisions of a "written contract" and that they expressly deal with payment of dividends.

Respectfully submitted,

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